

State of Illinois
Department of Employment Security

Individual Nonshared Governmental Funds
Individual Nonshared Proprietary Fund
Financial Statements
For the Year Ended June 30, 2009
Performed as Special Assistant Auditors
for the Auditor General, State of Illinois

State of Illinois
Department of Employment Security

Financial Audits
For the Year Ended June 30, 2009

Table of Contents

	<u>Page(s)</u>
Agency Officials	1
<u>Individual Nonshared Governmental Funds:</u>	
Financial Statement Report Summary	2
Independent Auditors' Report	3-4
Individual Nonshared Governmental Fund Financial Statements:	
Balance Sheets	5
Statements of Revenues, Expenditures and Changes in Fund Balances	6
Notes to Financial Statements	7-18
Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	19-20
<u>Individual Nonshared Proprietary Fund:</u>	
Financial Statement Report Summary	21
Independent Auditors' Report	22-23
Individual Nonshared Proprietary Fund Financial Statements:	
Statement of Net Assets	24
Statement of Revenues, Expenses and Changes in Net Assets	25
Statement of Cash Flows	26-27
Notes to Financial Statements	28-36
Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	37-38
Schedule of Findings	39-44
Prior Finding Not Repeated	45

**STATE OF ILLINOIS
DEPARTMENT OF EMPLOYMENT SECURITY**

Individual Nonshared Governmental Funds

Financial Statements

For the Year Ended June 30, 2009

**Performed as Special Assistant Auditors
for the Auditor General, State of Illinois**

**State of Illinois
Department of Employment Security**

**Agency Officials
June 30, 2009**

Director	
Previous to August 25, 2008	Mr. James P. Sledge
August 25, 2008 to present	Ms. Maureen T. O'Donnell
Deputy Director, Administration	
Previous to August 26, 2008	Ms. Elizabeth Nicholson
September 22, 2008 to present	Ms. Theresa Larkin
Deputy Director, Operations	
Previous to September 3, 2009	Ms. LaToya Price-Childs
November 1, 2009 to present	Mr. Andrew Fox
Deputy Director, Infrastructure and Communications	
January 20, 2009 to present	Mr. Antonio Daniels
Chief Financial Officer	Mr. Jon Gingrich
Chief Information Services Officer	Mr. Thomas Revane
Manager, Revenue Division	Ms. Lois Cuevas
Manager, Workforce Development	
Previous to January 1, 2010	Ms. Virginia Long
General Counsel	Mr. Joseph P. Mueller
Manager, Accounting Services Division	Mr. L. Briant Coombs
Manager, Economic Information & Analysis Division	
Acting, previous to June 1, 2008	Mr. Mitch Daniels
June 1, 2008 to present	Dr. Evelina Tainer Loescher
Manager, General Services Division	Mr. John Rogers
Manager, Human Resources	Mr. Ken Santiago
Manager, Unemployment Insurance Division	Ms. Carolyn Vanek
Manager, Employment Services Division	
Previous to July 23, 2009	Mr. Bennett Krause
Employment Services, Education & Events	
July 23, 2009 to present	Ms. Kisha Hart
Employer & Community Outreach	
July 23, 2009 to present	Mr. Bennett Krause
Manager, Strategic Planning	
Previous to August 6, 2008	Ms. Georgina Heard-LaBonne
August 6, 2008 to present	Ms. Kisha Hart
Equal Opportunity Officer	Mr. Carlos Charneco

The Department's Administrative offices are located at:

33 South State Street
Chicago, IL 60603-2802

850 East Madison Street
Springfield, IL 62702-5603

**State of Illinois
Department of Employment Security**

**Financial Statements
For the Year Ended June 30, 2009**

FINANCIAL STATEMENT REPORT SUMMARY

The audit of the accompanying individual nonshared governmental fund financial statements of the State of Illinois, Department of Employment Security (Department) was performed by E. C. Ortiz & Co., LLP.

Based on their audits, the auditors expressed unqualified opinions on the Department's individual nonshared governmental fund financial statements.

SUMMARY OF FINDING

The auditors identified a matter involving the Department's internal control over financial reporting that they considered to be a significant deficiency. The significant deficiency is described in the accompanying Schedule of Findings on pages 42-44 of this report, as finding 09-3.

EXIT CONFERENCE

The finding and recommendation appearing in the report were discussed with Department personnel at an exit conference on January 6, 2010. Attending were:

Illinois Department of Employment Security

Chicago Office

Maureen O'Donnell, Director
Theresa Larkin, Administration Deputy Director
Antonio Daniels, Infrastructure & Communications
Deputy Director
Andy Fox, Operations Deputy Director
Jon Gingrich, Chief Financial Officer
Briant Coombs, Accounting Services Division Manager
Barry Isaacson, IS Administrative Services Subdivision Manager
Letitia Dominici, Senior Policy Advisor
Carlos Charneco, Equal Opportunity Officer
Kathy Harlan, Audit Liaison

Springfield Office

Joseph Mueller, General Counsel
Carolyn Vanek, Unemployment Insurance
Division Manager
Jim Preckwinkle, Legislative Liaison

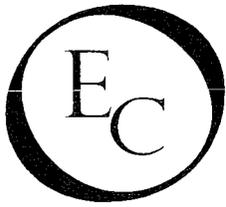
E. C. Ortiz & Co., LLP

Edilberto Ortiz, Partner
Jennifer Santos, Partner
Annabelle Abueg, IS Audit Manager
Epifanio Sadural, Manager

Office of the Auditor General

Thomas Kizziah, Audit Manager
Kathleen A. Devitt, IS Audit Manager

The response to the recommendation was provided by Kathy Harlan in a letter dated January 12, 2010.



INDEPENDENT AUDITORS' REPORT

Honorable William G. Holland
Auditor General
State of Illinois

As Special Assistant Auditors for the Auditor General, we have audited the accompanying financial statements of the Title III Social Security and Employment Services Fund, Unemployment Compensation Special Administration Fund, and Special Programs Fund (Nonshared Governmental Funds) of the State of Illinois, Department of Employment Security (Department), as of and for the year ended June 30, 2009, as listed in the table of contents. These financial statements are the responsibility of the Department's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 2 the financial statements present only the Nonshared Governmental Funds and do not purport to, and do not, present fairly the financial position of the Department as of June 30, 2009, and its changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Nonshared Governmental Funds of the Department, as of June 30, 2009, and the changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated January 12, 2010 on our consideration of the Department's internal control over financial reporting of the Nonshared Governmental Funds and on our tests of the Department's compliance with certain provisions of laws, regulations, contracts and, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Department has not presented a management's discussion and analysis for the Nonshared Governmental Funds that accounting principles generally accepted in the United States of America has determined is necessary to supplement, although not required to be part of, the financial statements.

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, the Comptroller, Department management, and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

E. C. Ortiz & Co., LLP

Chicago, Illinois
January 12, 2010

State of Illinois
Department of Employment Security

Individual Nonshared Governmental Funds

Balance Sheets

June 30, 2009

(Amounts in \$000's)

	Title III Social Security and Employment Services Fund	Unemployment Compensation Special Administration Fund	Special Programs Fund
Assets			
Cash and cash equivalents	\$ 3,626	\$ 12,569	\$ -
Intergovernmental receivables	28,852	-	111
Other receivables	1	2	-
Due from other State funds	18,384	1,807	-
Inventories	728	-	-
Total assets	<u>\$ 51,591</u>	<u>\$ 14,378</u>	<u>\$ 111</u>
Liabilities and Fund Balances			
Liabilities:			
Accounts payable and accrued liabilities	\$ 9,769	\$ 106	\$ 111
Intergovernmental payables	351	-	-
Due to other State funds	13,130	-	-
Total liabilities	<u>23,250</u>	<u>106</u>	<u>111</u>
Fund Balances:			
Reserved for inventories	728	-	-
Unreserved - undesignated	27,613	14,272	-
Total fund balances	<u>28,341</u>	<u>14,272</u>	<u>-</u>
Total liabilities and fund balances	<u>\$ 51,591</u>	<u>\$ 14,378</u>	<u>\$ 111</u>

See Notes to Financial Statements.

State of Illinois
Department of Employment Security

Individual Nonshared Governmental Funds
Statements of Revenues, Expenditures, and Changes in Fund Balances
Year Ended June 30, 2009
(Amounts in \$000's)

	Title III Social Security and Employment Services Fund	Unemployment Compensation Special Administration Fund	Special Programs Fund
Revenues			
Federal government	\$ 219,464	\$ -	\$ 5,659
Other revenues	1,435	-	-
Licenses and fees	19	-	-
Interest and investment income	151	66	-
Total revenues	<u>221,069</u>	<u>66</u>	<u>5,659</u>
Expenditures			
Employment and economic development	222,357	2,118	5,659
Capital outlays	41	-	-
Total expenditures	<u>222,398</u>	<u>2,118</u>	<u>5,659</u>
Deficiency of revenues under expenditures	<u>(1,329)</u>	<u>(2,052)</u>	<u>-</u>
Other financing sources (uses)			
Transfers in	12,014	13,207	-
Transfers out	-	(13,519)	-
Total other financing sources (uses)	<u>12,014</u>	<u>(312)</u>	<u>-</u>
Net changes in fund balances	10,685	(2,364)	-
Fund balances, July 1, 2008	<u>17,656</u>	<u>16,636</u>	<u>-</u>
Fund balances, June 30, 2009	<u>\$ 28,341</u>	<u>\$ 14,272</u>	<u>\$ -</u>

See Notes to Financial Statements.

**State of Illinois
Department of Employment Security**

**Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

1. Description of Funds

The State of Illinois, Department of Employment Security (the Department) administers the nonshared governmental funds described below. A nonshared fund is a fund in which a single State agency is responsible for administering substantially all financial transactions of the fund. The nonshared funds administered by the Department are summarized below.

- (a) Title III Social Security and Employment Services Fund** - The Department is organized to administer grant and program activities under various federal mandates, statutes and regulations. This fund accounts for all general disbursements for the everyday operation of the Department.
- (b) Unemployment Compensation Special Administration Fund** - This fund accounts for collections of interest and penalties from employers and judgment interest from claimants. Funds are used as provided by law as necessary for the proper administration of the Unemployment Insurance Act or transferred to the Unemployment Compensation Trust Fund.
- (c) Special Programs Fund** - This fund accounts for paying unemployment benefits under the Trade Readjustment Act program (TRA), Alternative Trade Adjustment Assistance (ATAA), and Disaster Unemployment Assistance (DUA).

2. Summary of Significant Accounting Policies

The financial statements of the individual nonshared governmental funds administered by the Department have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), as prescribed by the Governmental Accounting Standards Board (GASB). To facilitate the understanding of data included in the financial statements, summarized below are the more significant accounting policies.

(a) Reporting Entity

As defined by GAAP, the financial reporting entity consists of the primary government, as well as its component units, which are legally separate organizations for which the elected officials of the primary government are financially accountable.

**State of Illinois
Department of Employment Security**

**Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

2. Summary of Significant Accounting Policies, continued

(a) Reporting Entity - continued

Financial Accountability is defined as:

- (1) Appointment of a voting majority of the component unit's board and either (a) the primary government's ability to impose its will, or (b) the possibility that the component unit will provide financial benefit to or impose a financial burden on the primary government; or
- (2) Fiscal dependency on the primary government.

Based upon the required criteria, none of the individual nonshared governmental funds have component units, nor is either one a component unit of any other entity. However, because the individual nonshared governmental funds are not legally separate from the State of Illinois, they are included in the financial statements of the State as governmental funds. The State of Illinois' Comprehensive Annual Financial Report may be obtained by writing to the State Comptroller's Office, Financial Reporting Department, 325 West Adams Street, Springfield, Illinois, 62704-1871.

The financial statements present only the Title III Social Security and Employment Services, Unemployment Compensation Special Administration, and Special Program Funds administered by the Department and do not purport to, and do not, present fairly the financial position of the Department as of June 30, 2009, and changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

(b) Basis of Presentation

In government, the basic accounting and reporting entity is a fund. A fund is defined as an independent fiscal and accounting entity with a self-balancing set of accounts recording cash and/or other resources together with all related liabilities, obligations, reserves, and equities which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations. A balance sheet and statement of revenues, expenditures, and changes in fund balance have been presented for each individual nonshared governmental fund administered by the Department.

Each of the nonshared governmental funds is a special revenue fund. Transactions related to resources obtained from specific revenue sources (other than for expendable trusts) that are legally restricted for specified purposes are accounted for in special revenue funds. Special revenue funds are not shared with other State agencies. The Department administers grant and program activities under various federal mandates, statutes and regulations. The major federally funded administrative activities conducted by the Department are accounted for in the Title III Social Security and Employment Service Fund.

**State of Illinois
Department of Employment Security**

**Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

2. Summary of Significant Accounting Policies, continued

(b) Basis of Presentation, continued

The Unemployment Compensation Special Administration Fund accounts for collections of interest and penalties from employers and judgment interest from claimants, and funds are used as provided by law as necessary for the administration of the Unemployment Insurance Act. The Special Programs Fund accounts for paying unemployment benefits under various federal programs.

All Special Revenue Funds are held in the State Treasury, except for the Special Programs Fund, which is held locally. The funds are appropriated by the General Assembly, except for certain expenditures of the Unemployment Compensation Special Administration Fund, which are excluded from appropriation by the Illinois Unemployment Insurance Act, and the unemployment benefits paid from the Special Programs Fund.

(c) Basis of Accounting

The individual nonshared governmental funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting.

Revenues are recognized as soon as they are both measurable and available. Nonexchange transactions, in which the Department gives (or receives) value without directly receiving (or giving) equal value in exchange, include grants from the federal and other state governments. Revenue from grants, entitlements, and similar items is recognized in the fiscal year in which all eligibility requirements imposed by the provider have been met and the resources are available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the State considers revenues to be available if they are collected within 60 days of the end of the current fiscal year.

Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, principal and interest on long-term debt obligations, claims and judgments, and compensated absences are recorded only when payment is due. General capital asset acquisitions are reported as expenditures. Proceeds of long-term debt obligations and acquisitions under capital leases are reported as other financing sources.

Significant revenue sources of the individual nonshared governmental funds which are susceptible to accrual include grants from the federal government. All other revenue sources including fees, interest, and investment income are considered to be measurable and available only when cash is received.

**State of Illinois
Department of Employment Security**

**Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

2. Summary of Significant Accounting Policies, continued

(d) Cash and Cash Equivalents

Cash and cash equivalents consist principally of deposits held in the State Treasury. Cash and cash equivalents also include cash on hand, cash in banks for locally held funds, and pooled investments funds held by other governmental agencies with a maturity of three months or less.

(e) Inventories

Inventories, consisting primarily of printed forms and supplies, are valued at cost. Inventories for each fund are recorded as expenditures when consumed rather than when purchased.

(f) Interfund Transactions

The individual governmental nonshared funds have the following types of interfund transactions with other funds of the State:

Services provided and used - sales and purchases of goods and services between funds for a price approximating their external exchange value. Interfund services provided and used are reported as revenues in seller funds and expenditures or expenses in purchaser funds. Unpaid amounts are reported as interfund receivables and payables in the fund balance sheets or fund statements of net assets.

Reimbursements - repayments from the funds responsible for particular expenditures or expenses to the funds that initially paid for them. Reimbursements are reported as expenditures in the reimbursing fund and as a reduction of expenditures in the reimbursed fund.

Operating transfers - flows of assets (such as cash or goods) without equivalent flows of assets in return and without a requirement for repayment. Transfers are reported as other financing uses in the funds making the transfers and as other financing sources in the funds receiving transfers.

(g) Compensated Absences

A liability for unpaid, accumulated vacation and sick leave balances for the Department employees is reported in the nonshared funds only if they have matured, for example, as a result of employee resignations and retirements. There was no liability for compensated absences as of June 30, 2009.

(h) Fund Balances

The individual nonshared governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for specific purpose. Designations of fund balances represent tentative State plans that are subject to change.

**State of Illinois
Department of Employment Security**

**Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

2. Summary of Significant Accounting Policies, continued

(i) Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

3. Deposits

The State Treasurer is the custodian of the State's cash and cash equivalents for funds maintained in the State Treasury. The Department independently manages cash and cash equivalents maintained outside the State Treasury.

Deposits in the custody of the State Treasurer (or in transit) and cash on hand at June 30, 2009, were as follows:

Fund	Deposits in Custody of State Treasurer	Cash On Hand
Title III Social Security and Employment Services	\$ 3,622	\$ 4
Unemployment Compensation Special Administration	12,569	-
	<u>\$ 16,191</u>	<u>\$ 4</u>

Deposits in the custody of the State Treasurer are pooled and invested with other State funds in accordance with the Deposit of State Moneys Act of Illinois Compiled Statutes (15 ILCS 520/11). Funds held by the State Treasurer have not been categorized as to credit risk because the Department does not own individual securities. Details on the nature of these investments are available within the State of Illinois' Comprehensive Annual Financial Report.

State of Illinois
Department of Employment Security

Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)

4. Interfund Balances and Activities

(a) Balances Due to/from Other Funds

The following balances at June 30, 2009 represent amounts due from other Department and State of Illinois funds.

Fund	Amount	Description/Purpose
Title III Social Security and Employment Services	\$ 3	Due from Unemployment Compensation Trust Fund representing discretionary transfers of NSF fees
	18,323	Due from Unemployment Trust Fund for the unexpended balance of Special Administrative Transfer for UI expenses
	5	Due from Department of Public Aid for weekly statistical services and monthly intercept of UI benefits
	53	Due from Department of Commerce and Economic Opportunity
Total	<u>\$ 18,384</u>	
Unemployment Compensation Special Administration	\$ 1,807	Due from Unemployment Compensation Trust Fund representing transfers of penalties and interest
Total	<u>\$ 1,807</u>	

**State of Illinois
Department of Employment Security**

**Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

4. Interfund Balances and Activities, continued

(a) Balances Due to/from Other Funds, continued

The following balances at June 30, 2009 represent amounts due to other Department and State of Illinois funds.

<u>Fund</u>	<u>Amount</u>	<u>Description/Purpose</u>
Title III Social Security and Employment Services	\$ 12	Due to Unemployment Compensation Trust Fund for reimbursement of unemployment benefits paid to former employees of the Department
	13,118	Due to other State funds for payment of services
Total	<u>\$ 13,130</u>	

State of Illinois
Department of Employment Security

Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)

4. Interfund Balances and Activities, continued

(a) Transfers to/from Other Funds

Interfund transfers in for the year ended June 30, 2009, were as follows:

Fund	Amount	Description/Purpose
Title III Social Security and Employment Services	\$ 12,000	Discretionary transfer of penalties and interest from Unemployment Compensation Special Administration Fund
	14	Discretionary transfer of NSF fees from Unemployment Compensation Trust Fund
Total	<u>\$ 12,014</u>	
Unemployment Compensation Special Administration	\$ 13,207	Discretionary transfer of penalties and interest from Unemployment Compensation Trust Fund
Total	<u>\$ 13,207</u>	

State of Illinois
Department of Employment Security

Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)

4. Interfund Balances and Activities, continued

(a) Transfers to/from Other Funds, continued

Interfund transfers out for the year ended June 30, 2009, were as follows:

Fund	Amount	Description/Purpose
Unemployment Compensation Special Administration	\$ 12,000	Discretionary transfer of funds to Title III Social Security and Employment Services Fund
	1,519	Mandatory transfer to reimburse Unemployment Trust fund for TRA Settlement Funding.
Total	<u>\$ 13,519</u>	

5. Pension Plan

Substantially all of the Department's full-time employees who are not eligible for participation in another state-sponsored retirement plan participate in the State Employees' Retirement System (SERS), which is a pension trust fund in the State of Illinois reporting entity. The SERS is a single-employer defined benefit public employee retirement system (PERS) in which State employees participate, except those covered by the State Universities, Teachers', General Assembly, and Judges' Retirement Systems. The financial position and results of operations of the SERS for fiscal year 2009 are included in the State of Illinois' Comprehensive Annual Financial Report (CAFR) for the year ended June 30, 2009. The SERS issues a separate CAFR that may be obtained by writing to the SERS, 2101 South Veterans Parkway, Springfield, Illinois, 62794-9255.

A summary of SERS benefit provisions, changes in benefit provisions, employee eligibility requirements including eligibility for vesting, and the authority under which benefit provisions are established are included as an integral part of the SERS' CAFR. Also included is a discussion of employer and employee obligations to contribute, and the authority under which those obligations are established.

The Department pays employer retirement contributions in the individual nonshared governmental funds based upon an actuarially determined percentage of their payrolls. For fiscal year 2009, the employer contribution rate was 21.049%.

**State of Illinois
Department of Employment Security**

**Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

6. Post-employment Benefits

The State provides health, dental, vision, and life insurance benefits for retirees and their dependents in a program administered by the Department of Healthcare and Family Services along with the Department of Central Management Services. Substantially all State employees become eligible for post-employment benefits if they eventually become annuitants of one of the State sponsored pension plans. Health, dental, and vision benefits include basic benefits for annuitants and dependents under the State's self-insurance plan and insurance contracts currently in force. Annuitants may be required to contribute towards health, dental, and vision benefits with the amount based on factors such as date of retirement, years of credited service with the State, whether the annuitant is covered by Medicare, and whether the annuitant has chosen a managed health care plan. Annuitants who retired prior to January 1, 1998, and who are vested in the State Employee's Retirement System do not contribute towards health, dental, and vision benefits. For annuitants who retired on or after January 1, 1998, the annuitant's contribution amount is reduced five percent for each year of credited service with the State allowing those annuitants with twenty or more years of credited service to not have to contribute towards health, dental, and vision benefits. Annuitants also receive life insurance coverage equal to the annual salary of the last day of employment until age 60, at which time the benefit becomes \$5.

The total cost of the State's portion of health, dental, vision, and life insurance benefits of all members, including post-employment health, dental, vision, and life insurance benefits, is recognized as expenditure by the State in the Illinois Comprehensive Annual Financial Report. The State finances the costs on a pay-as-you-go basis. The total costs incurred for health, dental, vision, and life insurance benefits are not separated by department or component unit for annuitants and their dependents, nor active employees and their dependents.

A summary of post-employment benefit provisions, changes in benefit provisions, employee eligibility requirements including eligibility for vesting, and the authority under which benefit provisions are established are included as an integral part of the financial statements of the Department of Healthcare and Family Services. A copy of the financial statements of the Department of Healthcare and Family Services may be obtained by writing to the Department of Healthcare and Family Services, 201 South Grand Ave., Springfield, Illinois, 62763-3838.

7. Risk Management

The Department is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omission; workers compensation and natural disasters. The State retains the risk of loss (i.e., self insured) for these risks. There has been no reduction in insurance coverage from coverage in the prior year. Settlement amounts have not exceeded coverage for the current or prior two fiscal years. The Department's risk management activities for workers compensation are financed through appropriations to the Illinois Department of Central Management Services and are accounted for in the General Fund of the State. The claims are not considered to be a liability of the Department and accordingly, have not been reported in the Department's financial statements for the year ended June 30, 2009.

**State of Illinois
Department of Employment Security**

**Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

8. Commitments and Contingencies

(a) Federal Funding

The Department receives federal grants, which are subject to review and audit by federal grantor agencies. Certain costs could be questioned as not being an eligible expenditure under the terms of the grants. At June 30, 2009, there were no material questioned costs that have not been resolved with the federal awarding agencies. However, questioned costs could still be identified during audits to be conducted in the future. Management of the Department believes there will be no material adjustments to the federal grants and, accordingly, has not recorded a provision for possible repayment.

(b) Litigation

The Department is routinely involved in a number of legal proceedings and claims that cover a wide range of matters. In the opinion of management, the outcome of these matters is not expected to have any material adverse effect on the financial position or results of operations of the Department.

9. American Recovery and Reinvestment Act (ARRA)

The American Recovery and Reinvestment Act was enacted on February 17, 2009. Under this ARRA, the Department is accountable in the implementation and submission of all required federal reports for the following programs.

(a) Temporary Federal Additional Compensation Program (FAC)

The FAC program provides a twenty-five dollars weekly supplement to the unemployment compensation paid to eligible claimants. Any associated administrative expenses are 100% federally funded. The Department incurred \$51 in administrative costs as of June 30, 2009.

(b) Emergency Unemployment Compensation (EUC 08)

Although EUC 08 was initiated prior to the enactment of ARRA in July 2008, ARRA extended and expanded the program. Associated administrative costs are federally funded. As of June 30, 2009, the Department incurred \$5,359 in administrative costs.

(c) Special Administrative Transfer for UI

This is a special transfer of \$21,511 to the Department's Unemployment Trust Fund (UTF) from the federal government to be used for administrative expenses, including the improvement of UI operations. As of June 30, 2009, amount expended totals \$3,188.

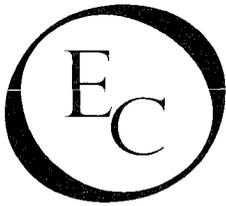
**State of Illinois
Department of Employment Security**

**Individual Nonshared Governmental Funds
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

9. American Recovery and Reinvestment Act (ARRA), continued

(d) Wagner-Peyser Act and Re-employment Services

This ARRA is a stimulus allotment for the Workforce Investment Act which includes the Wagner-Peyser Act and Re-employment Services. This program is intended to preserve and create jobs, to meet the needs of workers and employers, to implement effective One-Stop service delivery strategies, and for the re-employment of UI claimants. The Department started implementation of this program in July 2009.



**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

Honorable William G. Holland
Auditor General
State of Illinois

As Special Assistant Auditors for the Auditor General, we have audited the financial statements of the Title III Social Security and Employment Services Fund, Unemployment Compensation Special Administration Fund, and Special Programs Fund (Nonshared Governmental Funds) of the State of Illinois, Department of Employment Security (Department), as of and for the year ended June 30, 2009, and have issued our report thereon dated January 12, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Department's internal control over financial reporting of the Nonshared Governmental Funds as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting of the Nonshared Governmental Funds that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in finding 09-3 in the accompanying schedule of findings that we consider to be a significant deficiency in internal control over financial reporting. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's Nonshared Governmental Funds financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We are currently conducting a State compliance examination of the Department as required by the Illinois State Auditing act. The results of that examination will be reported to management under separate cover.

The Department's response to the finding identified in our audit is described in the accompanying schedule of findings. We did not audit the Department's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, Department management, and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

E. C. Ortiz + Co., LLP

Chicago, Illinois
January 12, 2010

**STATE OF ILLINOIS
DEPARTMENT OF EMPLOYMENT SECURITY**

Individual Nonshared Proprietary Fund

Financial Statements

For the Year Ended June 30, 2009

**Performed as Special Assistant Auditors
for the Auditor General, State of Illinois**

**State of Illinois
Department of Employment Security**

**Financial Statements
For the Year Ended June 30, 2009**

FINANCIAL STATEMENT REPORT SUMMARY

The audit of the accompanying individual nonshared proprietary fund financial statements of the State of Illinois, Department of Employment Security (Department) was performed by E. C. Ortiz & Co., LLP.

Based on their audit, the auditors expressed an unqualified opinion on the Department's individual nonshared proprietary fund financial statements.

SUMMARY OF FINDINGS

The auditors identified a matter involving the Department's internal control over financial reporting that they considered to be significant deficiencies. The significant deficiencies are described in the accompanying Schedule of Findings on pages 39-44 of this report, as findings 09-1 to 09-3. The auditors also consider finding 09-1 to be a material weakness.

EXIT CONFERENCE

The findings and recommendations appearing in the report were discussed with Department personnel at an exit conference on January 6, 2010. Attending were:

Illinois Department of Employment Security

Chicago Office

Maureen O'Donnell, Director
Theresa Larkin, Administration Deputy Director
Antonio Daniels, Infrastructure & Communications
Deputy Director
Andy Fox, Operations Deputy Director
Jon Gingrich, Chief Financial Officer
Briant Coombs, Accounting Services Division Manager
Barry Isaacson, IS Administrative Services Subdivision Manager
Letitia Dominici, Senior Policy Advisor
Carlos Charneco, Equal Opportunity Officer
Kathy Harlan, Audit Liaison

Springfield Office

Joseph Mueller, General Counsel
Carolyn Vanek, Unemployment Insurance
Division Manager
Jim Preckwinkle, Legislative Liaison

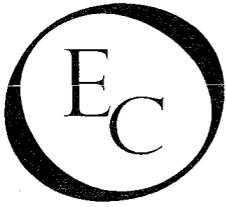
E. C. Ortiz & Co., LLP

Edilberto Ortiz, Partner
Jennifer Santos, Partner
Annabelle Abueg, IS Audit Manager
Epifanio Sadural, Manager

Office of the Auditor General

Thomas Kizziah, Audit Manager
Kathleen A. Devitt, IS Audit Manager

The responses to the recommendations were provided by Kathy Harlan in a letter dated January 12, 2010.



INDEPENDENT AUDITORS' REPORT

Honorable William G. Holland
Auditor General
State of Illinois

As Special Assistant Auditors for the Auditor General, we have audited the accompanying financial statements of the Unemployment Compensation Trust Fund (Nonshared Proprietary Fund) of the State of Illinois, Department of Employment Security (Department), as of and for the year ended June 30, 2009, as listed in the table of contents. These financial statements are the responsibility of the Department's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 2 the financial statements present only the Unemployment Compensation Trust Fund and do not purport to, and do not, present fairly the financial position of the Department as of June 30, 2009, and its changes in financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Unemployment Compensation Trust Fund of the Department, as of June 30, 2009, and the changes in financial position and cash flows, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 11, in July of 2009, the State of Illinois began receiving repayable advances to the account of the Illinois Unemployment Compensation Trust Fund (UTF) from the federal unemployment account in such fund. The UTF account, from which funds are drawn by the Department to pay unemployment benefits to claimants, was depleted due to extended high unemployment rates during the course of the current recession and tax revenues that have not matched the increased level of payments. Absent a robust economic recovery and/or legislative changes to the system, the Department projects that borrowing for the State will continue through at least 2012.

In accordance with *Government Auditing Standards*, we have also issued a report dated January 12, 2010 on our consideration of the Department's internal control over financial reporting of the Unemployment Compensation Trust Fund and on our tests of the Department's compliance with certain provisions of laws, regulations, contracts and, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Department has not presented a management's discussion and analysis for the Unemployment Compensation Trust Fund that accounting principles generally accepted in the United States of America has determined is necessary to supplement, although not required to be part of, the financial statements.

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, the Comptroller, Department management, and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

E. C. Ortiz + Co., LLP

Chicago, Illinois
January 12, 2010

State of Illinois
Department of Employment Security

Individual Nonshared Proprietary Fund

Statement of Net Assets

June 30, 2009

(Amounts in \$000's)

	<u>Unemployment Compensation Trust Fund</u>
Current Assets	
Cash and cash equivalents	\$ 92,790
Deposits held by federal government	183,115
Receivables, net:	
Taxes	353,635
Intergovernmental	107,914
Other	109,459
Due from State funds	12,018
Due from component units of the State of Illinois	<u>267</u>
Total current assets	<u>859,198</u>
Current Liabilities	
Benefit payments payable	227,399
Intergovernmental payables	11,509
Due to other State funds	<u>20,133</u>
Total current liabilities	<u>259,041</u>
Net Assets	
Restricted for unemployment compensation benefits	<u>600,157</u>
Total net assets	<u>\$ 600,157</u>

See Notes to Financial Statements.

State of Illinois
Department of Employment Security

Individual Nonshared Proprietary Fund
Statement of Revenues, Expenses, and Changes in Net Assets
Year Ended June 30, 2009
(Amounts in \$000's)

	<u>Unemployment Compensation Trust Fund</u>
Operating revenues:	
Contributions - unemployment taxes	\$ 1,600,817
Federal government	<u>1,644,757</u>
Total operating revenues	3,245,574
Operating expenses	
Benefit payments and refunds	<u>5,086,053</u>
Operating loss	<u>(1,840,479)</u>
Nonoperating revenues	
Interest and investment income	<u>61,180</u>
Total nonoperating revenues	<u>61,180</u>
Loss before transfers:	(1,779,299)
Transfers in	1,519
Transfers out	<u>(13,221)</u>
Decrease in net assets	(1,791,001)
Net assets, July 1, 2008	<u>2,391,158</u>
Net assets, June 30, 2009	<u>\$ 600,157</u>

See Notes to Financial Statements.

State of Illinois
Department of Employment Security

Individual Nonshared Proprietary Fund
Statement of Cash Flows
Year Ended June 30, 2009
(Amounts in \$000's)

	Unemployment Compensation Trust Fund
Cash flows from operating activities	
Contributions - unemployment taxes received	\$ 1,666,148
Federal grants received	1,610,166
Unemployment benefits paid	(4,954,040)
Net cash used in operating activities	<u>(1,677,726)</u>
Cash flows from noncapital financing activities	
Transfers in	1,519
Transfers out	(15,736)
Net cash used in noncapital financing activities	<u>(14,217)</u>
Cash flows from investing activities	
Interest and investment income	61,180
Net cash provided by investing activities	<u>61,180</u>
Net decrease in cash and cash equivalents	(1,630,763)
Cash and cash equivalents, July 1, 2008	<u>1,906,668</u>
Cash and cash equivalents, June 30, 2009	<u>\$ 275,905</u>
 <i>Reconciliation of cash and cash equivalents to the Statement of Net Assets</i>	
Total cash and cash equivalents per Statement of Net Assets	\$ 92,790
Add: Deposits held by federal government	183,115
Cash and cash equivalents, June 30, 2009	<u>\$ 275,905</u>

State of Illinois
Department of Employment Security

Individual Nonshared Proprietary Fund
Statement of Cash Flows - Continued
Year Ended June 30, 2009
(Amounts in \$000's)

	Unemployment Compensation Trust Fund
Reconciliation of operating income to net cash used in operating activities	
Operating loss	\$ (1,840,479)
Adjustments to reconcile operating income to net cash used in operating activities:	
Provision for uncollectible accounts	47,601
Changes in assets and liabilities	
Receivables	45,652
Intergovernmental receivables	(77,028)
Due from other funds	(7,373)
Due from component units	(94)
Benefit payments payable	130,586
Intergovernmental payables	5,086
Due to other funds	18,323
Net cash used in operating activities	<u><u>\$ (1,677,726)</u></u>

See Notes to Financial Statements.

**State of Illinois
Department of Employment Security**

**Individual Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

1. Description of Fund

The State of Illinois, Department of Employment Security (the Department) administers the nonshared proprietary fund as described below. A nonshared fund is a fund in which a single State agency is responsible for administering substantially all financial transactions of the fund.

The Unemployment Compensation Trust Fund accounts for assets held by the Department in a trustee capacity, for which the principal and income may be expended in the course of the fund's designated operations. The fund, a locally held fund, receives employer contributions and disburses money in the form of unemployment benefits paid to eligible claimants. This fund also receives federal funding to pay eligible claimants for any federally mandated benefit programs. The Unemployment Compensation Trust Fund is not appropriated by the General Assembly and is intended to be self-supporting.

2. Summary of Significant Accounting Policies

The financial statements of the individual nonshared proprietary fund has been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), as prescribed by the Governmental Accounting Standards Board (GASB). To facilitate the understanding of data included in the financial statements, summarized below are the more significant accounting policies.

(a) Reporting Entity

As defined by GAAP, the financial reporting entity consists of a primary government, as well as its component units, which are legally separate organizations for which the elected officials of the primary government are financially accountable. Financial accountability is defined as:

- (1) Appointment of a voting majority of the component unit's board and either (a) the primary government's ability to impose its will, or (b) the possibility that the component unit will provide financial benefit to or impose a financial burden on the primary government; or
- (2) Fiscal dependency on the primary government.

Based upon the required criteria, the individual nonshared proprietary fund does not have component units, nor is a component unit of any other entity. However, because the individual nonshared proprietary fund is not legally separate from the State of Illinois, it is included in the financial statements of the State as a proprietary fund. The State of Illinois' Comprehensive Annual Financial Report may be obtained by writing to the State Comptroller's Office, Financial Reporting Department, 325 West Adams Street, Springfield, Illinois, 62704-1871.

The financial statements include only the Unemployment Compensation Trust Fund administered by the Department and do not purport to, and do not, present fairly the financial position of the Department as of June 30, 2009, and changes in its financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

State of Illinois
Department of Employment Security

Individual Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)

2. Summary of Significant Accounting Policies, continued

(b) Basis of Presentation

In government, the basic accounting and reporting entity is a fund. A fund is defined as an independent fiscal and accounting entity with a self-balancing set of accounts recording cash and/or other resources together with all related liabilities, obligations, reserves, and equities which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations. A statement of net assets, statement of revenues, expenses, and changes in net assets, and statement of cash flows have been presented for the nonshared proprietary funds administered by the Department.

The nonshared proprietary fund is an enterprise fund. Enterprise funds are used to report any activity for which a fee is charged to external users for goods and services. Activities are required to be reported as enterprise funds if any one of the following criteria is met when applied in the context of the activity's principal revenue sources: the activity is financed with debt that is secured solely by a pledge of net revenues from fees and charges of the activity, laws and regulations require that the activity's costs of providing service, including capital costs, be recovered with fees and charges, rather than taxes or similar revenues, or the pricing policy of the activity establishes fees and charges designed to recover its costs, including capital costs.

The Department administers the unemployment insurance program under various federal and state statutes and regulations. The Unemployment Trust Fund was established under Title IX of the Social Security Act to provide partial protection to workers against the loss of wages when they are out of work due to no fault of their own. To fund this program, the agency receives monies from employers to maintain the fund used to pay benefits to the unemployed workers who meet the eligibility requirements of the law.

These funds are held by the United States Treasury in an unemployment trust fund and are restricted to the payment of unemployment benefits. Unemployment benefits drawn from the fund are awarded to qualified former employees of covered Illinois employers. Employers required to contribute to the unemployment trust fund do so based on employees' wages and past experience level of unemployment caused by the employing unit. The overall rate used to determine contributions for the Illinois Unemployment Insurance Trust Fund is designed to recover the payment of unemployment benefits plus maintain a reasonable balance to protect the solvency of the fund if unemployment rates rise significantly.

Operating revenues, such as collections of unemployment tax contributions, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as investment earnings, result from nonexchange transactions or ancillary activities.

State of Illinois
Department of Employment Security

Individual Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)

2. Summary of Significant Accounting Policies, continued

(c) Basis of Accounting

The individual nonshared proprietary fund is reported using the economic resources measurement focus and the accrual basis of accounting.

Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flow takes place. Nonexchange transactions, in which the Department gives (or receives) value without directly receiving (or giving) equal value in exchange, include federal funding for federally mandated benefit programs. On an accrual basis, revenues from employer contributions are recognized in the fiscal year in which the underlying exchange transaction occurs. Revenues from grants, entitlements, and similar items are recognized in the fiscal year in which all eligibility requirements imposed by the provider have been met.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally followed in the individual nonshared proprietary funds financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The State also has the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The State has elected not to follow subsequent private-sector guidance for the individual nonshared proprietary fund administered by the Department.

(d) Cash and Cash Equivalents

Cash and cash equivalents consist principally of cash in banks for locally held funds, U.S. government securities, and pooled investment funds held by other governmental agencies with a maturity of three months or less.

(e) Interfund Transactions

The individual nonshared proprietary fund has the following types of interfund transactions with other funds of the State:

Reimbursements - repayments from the funds responsible for particular expenditures or expenses to the funds that initially paid for them. Reimbursements are reported as expenditures in the reimbursing fund and as a reduction of expenditures in the reimbursed fund.

Transfers - flows of assets (such as cash or goods) without equivalent flows of assets in return and without a requirement for repayment. Transfers are reported after nonoperating revenues and expenses.

State of Illinois
Department of Employment Security

Individual Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)

2. Summary of Significant Accounting Policies, continued

(f) Net Assets

Net assets consist of the following:

Restricted net assets, totaling \$600,157 as of June 30, 2009, consist of net assets that are legally restricted by outside parties or by law through constitutional provisions or enabling legislation.

Unrestricted net assets consist of net assets that do not meet the criteria of the preceding category.

When both restricted and unrestricted resources are available for use, generally it is the State's policy to use restricted resources first, then unrestricted resources when they are needed.

(g) Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

3. Deposits

Cash and cash equivalents as of June 30, 2009 have a carrying amount in the accompanying financial statements of \$92,790.

At June 30, 2009, cash on deposit for the Unemployment Compensation Trust Fund (UTF) for locally held funds has a carrying amount of \$3,560 and the bank balance was \$3,552. The bank balance of \$3,552 was fully insured by the Federal Depository Insurance Corporation (FDIC) through the bank's participation in the Temporary Liquidity Guarantee Program. Deposits in Illinois Funds and in the custody of the State Treasurer for the UTF totaled \$89,936 and have a carrying amount of \$89,230 at June 30, 2009.

The State Treasurer is the custodian of the State's cash and cash equivalents for funds maintained in the State Treasury. The Department independently manages cash and cash equivalents maintained outside the State Treasury. The State of Illinois' Comprehensive Annual Financial Report may be obtained by writing to the State Comptroller's Office, Financial Reporting Department, 325 West Adams Street, Springfield, Illinois, 62704-1871.

Funds deposited in Illinois Funds and held by the State Treasurer are pooled and invested with other State funds in accordance with the Deposit of State Moneys Act of Illinois Compiled Statute (15 ILCS 520/11). These deposits have not been categorized as to credit risk because the Department does not own individual securities. Detail on the nature of these investments is available within the State of Illinois' Comprehensive Annual Financial Report.

State of Illinois
Department of Employment Security

Individual Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)

3. Deposits, continued

Illinois Funds is not registered with the SEC as an investment company, but does operate in a manner consistent with Rule 2a7 of the Investment Company Act of 1940. Investments in Illinois Funds are valued at Illinois Fund's share price, which is the price the investment could be sold for.

Deposits held by federal government totaled \$183,115 at June 30, 2009. These deposits are pooled and invested with other States' funds and have not been categorized as to credit risk because the Department does not own individual securities.

4. Taxes Receivable

Taxes receivable represent unemployment taxes, known as contributions, owed by private and non-governmental employers. The allowance for uncollectible taxes has been based on historical collection experience which, per statute, is typically on a 4 year collection cycle. Balances as of June 30, 2009, are as follows:

Taxes receivable:

Unemployment taxes	\$ 429,847
Interest and penalties receivable on taxes	<u>49,376</u>
Total taxes receivable	479,223
Less: allowance for uncollectible taxes	<u>(125,588)</u>
Taxes receivable	<u>\$ 353,635</u>

5. Intergovernmental Receivables

Intergovernmental receivables represent reimbursements due from other State and local governments for unemployment benefits paid to those government's ex-employees by the Trust Fund totaling \$107,914 as of June 30, 2009.

**State of Illinois
Department of Employment Security**

**Individual Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

6. Other Receivables

Other receivables represent amounts due from claimants who received benefits, which exceeded the allowable amounts. The allowance for uncollectible accounts has been based on historical collection experience which, per statute, is typically on a 4 year collection cycle.

Balances as of June 30, 2009 are as follows:

Other receivables	\$ 343,193
Less: allowance for uncollectible accounts	<u>(233,734)</u>
Other receivables, net	<u><u>\$ 109,459</u></u>

7. Interfund Balances and Activities

(a) Balances Due to/from Other Funds

The following balances at June 30, 2009 represent amounts due from other Department and State of Illinois funds.

Fund	Amount	Description/Purpose
Unemployment Compensation Trust Fund	\$ 12,004	Due from General Revenue Fund for reimbursement of unemployment benefits paid to employees of other State agencies
	12	Due from Title III Social Security and Employment Service Fund for the reimbursement of unemployment benefits to former employees of the Department
	2	Due from IL Math & Science Academy for the reimbursement of unemployment benefits to former employees
Total	<u><u>\$ 12,018</u></u>	

Due from component units of the State of Illinois of which \$267 represents reimbursement of unemployment benefits paid to employees of State universities.

**State of Illinois
Department of Employment Security**

**Individual Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

7. Interfund Balances and Activities, continued

(a) Balances Due to/from Other Funds, continued

The following balances at June 30, 2009 represent amounts due to other Department and State of Illinois funds.

Fund	Amount	Description/Purpose
Unemployment Compensation Trust Fund	\$ 3	Due to Title III Social Security and Employment Services Fund for discretionary transfers of NSF fees
	18,323	Due to Title III Social Security and Employment Services for the unexpended balance of Special Administrative Transfer for UI expenses
	1,807	Due to Unemployment Compensation Special Administration Fund for discretionary transfers of penalties and interests
Total	<u>\$ 20,133</u>	

(b) Transfers to/from Other Funds

Interfund transfers in for the year ended June 30, 2009, were as follows:

Fund	Amount	Description/Purpose
Unemployment Compensation Trust Fund	<u>\$ 1,519</u>	Transfer from Special Administration Fund 055 for reimbursement of TRA settlement

**State of Illinois
Department of Employment Security**

**Individual Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

7. Interfund Balances and Activities, continued

(b) Transfers to/from Other Funds, continued

Interfund transfers out for the year ended June 30, 2009, were as follows:

Fund	Amount	Description/Purpose
Unemployment Compensation Trust Fund	\$ 13,207	Discretionary transfers of penalties and interests to Unemployment Compensation Special Administration Fund
	14	Discretionary transfers of NSF fees to Title III Social Security and Employment Services Fund
Total	<u>\$ 13,221</u>	

8. Intergovernmental Payables

Intergovernmental payables of \$11,509 represent interstate combined wage claim benefits payable.

9. Contingencies

While the Department is involved in various claims and legal actions arising in the ordinary course of business, it is the opinion of management that the ultimate disposition of these matters will not have a material effect on the individual nonshared proprietary funds financial statements.

10. American Recovery and Reinvestment Act (ARRA)

The American Recovery and Reinvestment Act was enacted on February 17, 2009. Under this ARRA, the Department is accountable in the implementation and submission of all required federal reports for the following programs.

(a) Temporary Federal Additional Compensation Program (FAC)

FAC program provides a twenty-five dollars weekly supplement to the unemployment compensation of eligible claimants. This program is 100% funded by the federal government. As of June 30, 2009, FAC paid a total amount of \$172,530 to claimants.

**State of Illinois
Department of Employment Security**

**Individual Nonshared Proprietary Fund
Notes to Financial Statements
June 30, 2009
(Amounts in \$000's)**

10. American Recovery and Reinvestment Act (ARRA), continued

(b) Emergency Unemployment Compensation (EUC 08)

EUC 08 is payable to eligible claimants who have exhausted their regular unemployment compensation. This ARRA program is funded with federal general revenues. As of June 30, 2009, EUC paid out to claimants amounts to \$152,862.

(c) Unemployment Compensation Modernization Incentive

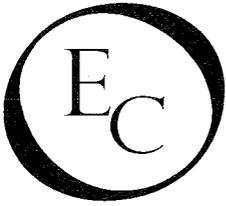
ARRA provided for incentive payments into state unemployment trust funds for states that had enacted specific provisions to modernize their unemployment statutes. As a result of having an alternate base period provision in its state law, Illinois received \$100,384 during FY09 to be used for the payment of future unemployment benefits.

(d) Extended Benefits (EB)

EB is a longstanding program that triggers on when certain economic conditions are met and provides additional weeks of benefits to claimants who exhaust their benefits under other unemployment programs. Although EB triggered on in Illinois during FY09 under previously existing federal and state law, ARRA made this traditionally 50% federally funded program into a virtually 100% federally funded program.

11. Subsequent Events

In July of 2009, the State of Illinois began receiving repayable advances to the account of the Illinois Unemployment Compensation Trust Fund (UTF) from the federal unemployment account in such fund. The UTF account, from which funds are drawn by the Department to pay unemployment benefits to claimants, was depleted due to extended high unemployment rates during the course of the current recession and tax revenues that have not matched the increased level of payments. As of December 31, 2009, a total of 26 states were borrowing from the Federal Government to fulfill the mandate to pay unemployment benefits and Illinois' loan balance was \$1,168,532. These loans are interest-free under current federal law through the end of calendar year 2010. Absent a robust economic recovery and/or legislative changes to the system, the Department projects that borrowing for the State will continue through at least 2012.



**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

Honorable William G. Holland
Auditor General
State of Illinois

As Special Assistant Auditors for the Auditor General, we have audited the financial statements the Unemployment Compensation Trust Fund (Nonshared Proprietary Fund) of the State of Illinois, Department of Employment Security (Department), as of and for the year ended June 30, 2009, and have issued our report thereon dated January 12, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Department's internal control over financial reporting of the Unemployment Compensation Trust Fund as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements and not for the purpose of expressing an opinion on the effectiveness of the Department's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in the internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of finding, we identified certain deficiency in internal control over financial reporting that we consider to be a material weakness.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in finding 09-1 in the accompanying schedule of findings to be a material weakness.

A *significant deficiency* is a deficiency or combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in findings 09-1 to 09-3 in the accompanying schedule of findings to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's Unemployment Compensation Trust Fund financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We are currently conducting a State compliance examination of the Department as required by the Illinois State Auditing act. The results of that examination will be reported to management under separate cover.

The Department's response to the finding identified in our audit is described in the accompanying schedule of findings. We did not audit the Department's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, Department management, and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

E. C. Ortiz & Co., LLP

Chicago, Illinois
January 12, 2010

**State of Illinois
Department of Employment Security**

**Schedule of Findings
For the Year Ended June 30, 2009**

Current Findings – *Government Auditing Standards*

09-1 Inaccurate Balance of Cash and Cash Equivalents and Benefit Payments Payable

The Department understated its cash and cash equivalents by \$43 million. The related benefit payments payable was also understated by the same amount.

During our audit, we noted that as of June 30, 2009, the Department recorded a transfer of funds amounting to \$43 million against cash and cash equivalents for benefit payments when the actual transfer was not made until July 1, 2009. This resulted to a corresponding understatement in the Department's benefit payments payable by the same amount. The financial statements and disclosures have been corrected for these adjustments.

Generally accepted accounting principles (GAAP) require that the transfer out of funds be recorded in the period the transaction is initiated. The Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires all State agencies to establish and maintain a system, or systems, of internal fiscal and administrative controls.

Department officials stated that the transfer was recorded on June 30, 2009 as it was the intention that the funds be transferred on that day. The Department accommodated the bank's request that the transfer be deferred until the following day.

Incorrect recording of transfers could result in a material misstatement to the financial statements. (Finding Code No. 09-1)

Recommendation

We recommend the Department evaluate its process and improve its controls over recording transactions in the correct fiscal year.

Department Response

We accept the recommendation. A new aspect of end-of-quarter processing due to FDIC changes was not properly communicated throughout IDES Accounting Services. This change has now been fully incorporated and communicated within IDES Accounting Services.

**State of Illinois
Department of Employment Security**

**Schedule of Findings
For the Year Ended June 30, 2009**

Current Findings – Government Auditing Standards, continued

09-2 Inadequate Controls Over Computer Security

The Department did not properly restrict the use of the Super ID access to its information systems.

The Information Services Bureau (ISB) was responsible for the development and maintenance of the Department's information systems and preserving the integrity and security of information warehoused within those systems. The Department processed approximately \$1.6 billion in employer unemployment tax revenue contributions and \$5 billion of unemployment payments in fiscal year 2009.

Managers of application development had access to the production environment. This access was granted through the use of Super IDs, which allowed full access to all production software and data tables in the production environment. The Department had issued five Super IDs. Four Super IDs were assigned to the Application Manager who supports Human Resources, Finance and the Revenue systems. One Super ID was assigned to the Applications Manager who supports the Benefits system. The managers allowed their staff to utilize these accounts by sharing the password.

During the audit period we found that ISB programmers shared and used Super IDs on a non-emergency basis in the production environment to resolve transactional or application-related problems. In a review of a system-generated log, we found that between December 29, 2008 and April 5, 2009, the Super ID was used 268 times. As a compensating control, the Support Services Division Manager compared the system log to an independent log which documented the use and approval for each instance of access to the production environment. We tested the independent log and found that they were properly completed for all 268 uses of the Super ID noted in the system log during that period.

According to the Department, staffing resources are often not available to follow the normal process for fixing errors, particularly errors occurring when converting benefit transactions from the Benefit Information System to the Benefit Charging System. The use of the Super ID is the expeditious method for ensuring that benefit transactions are processed correctly in BIS. Correcting such errors is critical as benefit charges are a key component of employer tax rate calculations.

The Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires all State agencies to establish and maintain a system, or systems, of internal fiscal controls and administrative controls. In addition, generally accepted information technology guidance endorses the development of adequate change control procedures to ensure proper segregation of duties. These procedures include restricting programmers from making a change and moving it into the production to ensure all changes have been independently authorized and moved to production.

The frequent use of the Super IDs increased the risk of unauthorized access to systems and data which could jeopardize the integrity of the Department's resources. Programming staff should generally be limited to accessing only the information specifically required to complete their assigned system development projects. Furthermore, Department policy stated that the use of the Super ID should be limited to the resolution of production problems when the Production Control Unit staff is either not scheduled or unavailable. (Finding Code No. 09-2, 08-2)

**State of Illinois
Department of Employment Security**

**Schedule of Findings
For the Year Ended June 30, 2009**

Current Findings – *Government Auditing Standards*, continued

Recommendation

We recommend the Department allocate the resources necessary to correct day-to-day transactional and applications related information systems problems without compromising the security of those systems by over utilizing Super ID access rights. Further, we recommend that the use of the Super ID be restricted to emergency uses as required by Department policy.

Department Response

We accept the recommendation. The Department will examine the resource implications of implementing the recommendation. Given the record volume of unemployment claimants in the current environment, the Department may occasionally need to use extraordinary measures in order to ensure timely service to claimants. In these cases, the Department will continue to leverage the compensating controls which are in place and currently provide detailed system access logs.

State of Illinois
Department of Employment Security

Schedule of Findings
For the Year Ended June 30, 2009

Current Findings – Government Auditing Standards, continued

09-3 Untimely Preparation and Review of Monthly Reconciliation Reports

The Department did not timely prepare and review the monthly reconciliation reports. In addition, reconciling items were not adequately supported and adjusted in the books timely.

During our test of controls, we noted the following monthly reconciliation reports were not prepared timely:

Title III Social Security and Employment Services Fund

- Two (2) Appropriation (SB01) Reports were late ranging from 9 to 24 days late;
- Three (3) Revenue Status (SB04) Reports were late ranging from 2 to 10 days late; and
- Four (4) Cash (SB05) Reports were late ranging from 2 to 22 days late.

Unemployment Compensation Special Administrative Fund

- Two (2) SB01 Reports were late ranging from 4 to 15 days late; and
- Four (4) SB05 Reports were late ranging from 2 to 22 days late.

Special Program Fund

- Five (5) bank reconciliations for Alternative Trade Adjustment Assistance (ATAA) Fund were late ranging from 5 to 62 days late;
- Six (6) bank reconciliations for Trade Readjustment Assistance(TRA) Fund were late ranging from 2 to 64 days late; and
- Five (5) bank reconciliations for Disaster Unemployment Assistance (DUA) Fund were late ranging from 5 to 62 days late.

Unemployment Compensation Trust Fund

- Three (3) bank reconciliations were late ranging from 9 to 19 days.
- Six (6) bank reconciliations were not dated by the preparer.

Also, we noted the following reconciliation reports were not reviewed timely:

Title III Social Security and Employment Services Fund

- Two (2) SB04 Reports were late ranging from 1 to 2 days late; and
- Two (2) SB05 Reports were late ranging from 1 to 2 days late.

Unemployment Compensation Special Administrative Fund

- Two (2) SB05 Reports were late ranging from 1 to 2 days late.

Special Program Fund

- Two (2) bank reconciliations were late ranging from 4 to 34 days for ATAA;
- Two (2) bank reconciliations were late ranging from 4 to 34 days for TRA; and
- Two (2) bank reconciliations were late ranging from 4 to 34 days for DUA.

**State of Illinois
Department of Employment Security**

**Schedule of Findings
For the Year Ended June 30, 2009**

Current Findings – *Government Auditing Standards*, continued

Unemployment Compensation Trust Fund

- One (1) bank reconciliation was late by 17 days.
- Four (4) bank reconciliations were not dated by the reviewer.

Further, we noted the following in the reconciliation for the Unemployment Compensation Trust Fund:

- Twelve (12) instances where the reconciliation had unadjusted recurring items.
- Twelve (12) instances where the reconciliation was not adequately supported.
- Four (4) instances where the reconciliation was approved with unaccounted differences.

The Department subsequently revised the monthly bank reconciliation for Unemployment Compensation Trust Fund to account, correct and adjust the reconciling items from December 2008 to May 2009.

Sound internal controls require bank reconciliations to be performed promptly. Reconciling items should be investigated and adjustments made to the general ledger on a timely basis.

Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires all State agencies to establish and maintain a system, or systems, of internal fiscal and administrative controls.

Department practice measures timeliness of preparation and review of monthly reconciliation for Title III Social Security and Employment Services Fund and Unemployment Compensation Special Administrative Fund to be two months after month-end and two months after quarter-end, respectively.

Good business practice measures timeliness of preparation and review of monthly reconciliation for Special Program Fund and Unemployment Compensation Trust Fund to be two months after month-end and three months after month-end, respectively.

Department officials stated that Administrative Funds (052, 055 and 1136) were not always prepared timely due to a staff shortage that existed throughout FY09. The longest delays occurred during GAAP preparation when priority was given to completing the reconciliations for the current fiscal year.

A daily reconciliation is performed of the Trust Fund (1138) bank account information using information from the Benefit Information System, Federal Reserve Bank (FRB) detail transactions and bank statements. The information from the systems was downloaded into the Paradox database program, balances were reviewed for accuracy and exceptions were returned to FRB or the bank responsible for the reconciling items. In addition, as a back-up method, a spreadsheet was created pulling the data from various sources to show the complete month's reconciliation of the ETA 8401 to the bank accounts, previously created in the Paradox program. The daily reconciliations of the bank statements were performed timely and the spreadsheet review of the ETA 8401 to the bank accounts were completed timely; however the back-up reconciliations took longer to finalize. The unadjusted recurring items were the cumulative cleared check discrepancy amounts that were under or over the \$25 FRB threshold. These amounts are carried forward each month until an adjustment is made to the Ledger that will clear the reconciling item.

**State of Illinois
Department of Employment Security**

**Schedule of Findings
For the Year Ended June 30, 2009**

Current Findings – *Government Auditing Standards*, continued

Failure to prepare and review bank reconciliations timely increases the risk that cash may be misappropriated or financial reports may be misstated and the Department would not detect the loss or errors on a timely basis. (Finding Code 09-3)

Recommendation

We recommend the Department prepare and review the monthly reconciliation reports on a timely basis. This should include the date that the reconciliation reports are prepared and reviewed.

Department Response

We accept the recommendation. As noted above, daily reconciliations were performed timely as were portions of the monthly reconciliations. Improvements to the timeliness of the back-up monthly reconciliations are anticipated as we continue to address the staffing issues that were the primary cause of the delays.

**State of Illinois
Department of Employment Security**

**Prior Finding Not Repeated
For the Year Ended June 30, 2009**

A. Inaccurate Balance of Allowance for Uncollectible Accounts

The Department overstated its allowance for uncollectible taxes receivable by \$24.2 million. The methodology utilized by the Department to calculate its allowance for uncollectible taxes, penalties, and interest receivable did not correlate with its known history of collecting these types of receivables. (Finding Code No. 08-1)

Status: Implemented

The current period testing did not disclose the same exception.